

GAO

Report to the Chairwoman,
Subcommittee on Government
Activities and Transportation,
Committee on Government Operations,
House of Representatives

December 1989

FEDERAL REAL PROPERTY

Conflicting Appraisals of Land Near Columbia Hospital for Women



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547227

General Government Division

B-236257

December 11, 1989

The Honorable Cardiss Collins
Chairwoman, Subcommittee on
Government Activities and Transportation
Committee on Government Operations
House of Representatives

Dear Madam Chairwoman:

This report responds to your request that we comment on the differences between two appraisals of the government-owned property located at 2400 M Street, N.W., in the District of Columbia. Your subcommittee is presently considering H.R. 2031. If enacted, this bill would direct the Administrator of General Services to sell this property to the Columbia Hospital for Women for \$7 million paid on the date of conveyance plus \$3 million paid 15 years after that date.

Background

We obtained an appraisal of the land, as the Chairman of the House Committee on the District of Columbia requested. In our report to the Chairman,¹ we said that our contract appraiser estimated that the special use value and fair market value of the property were \$8,550,000 on December 31, 1981, and were \$20,000,000 on October 31, 1988. Our appraiser defined the special use value as the marketable measure of the value of the property to the Columbia Hospital for Women for certain hospital-related purposes, such as a clinic, a rehabilitation center, or a medical research institution.

The President and Chief Executive Officer of the Columbia Hospital for Women obtained a second appraisal. This appraisal estimated the market value of the property as of February 22, 1989, to be \$9,000,000, or only 45 percent of the special use value and fair market value arrived at by our appraiser as of October 31, 1988. The second appraisal did not consider the property's 1981 value.

Results in Brief

The principal difference between the two appraisals is that the first appraisal was prepared in accordance with federal appraisal standards, while the second was not. The first appraisal based the fair market value on the highest and best use of the land, in accordance with federal

¹ Federal Real Property: Appraisal of Land to Be Sold to Columbia Hospital for Women (GAO/ GGD-89-46, Mar. 10, 1989).

policy. The second appraisal did not and based the market value of the land on the development currently being proposed for the property by the Columbia Hospital for Women. Columbia Hospital's proposed underdevelopment of the property represents an opportunity cost to Columbia Hospital. We believe that the fair market value of the property should reflect the highest and best use and the fact that unused development rights could be used at a later date. After examining both appraisals, we believe that the first appraisal represents a reasonable and appropriate estimate of the property's fair market value on the indicated dates.

Approach and Criteria

We limited our work to analyzing the appraisal commissioned by Columbia Hospital for Women, which was included with your request, and to comparing its contents with those in our previous report. We also discussed the technical aspects of the appraisals with our contract appraiser and the Chief Appraiser, Office of Real Estate Policy and Sales, General Services Administration. We did not meet with Columbia Hospital officials, its appraiser, or any other interested parties. We did our work from June to October 1989.

In evaluating the appraisals and developing our conclusion, we followed the appraisal standards described in the Uniform Appraisal Standards for Federal Land Acquisitions (Standards), the court decisions cited in that publication, and the General Services Administration's Appraisal of Excess and Surplus Real Property Handbook. The second appraisal was prepared for a private client and consequently did not have to adhere to these federal standards.

The principal standards we used in reviewing the different approaches taken in valuing the property and the resulting appraisal reports follow:

Fair market value criterion. Under established law, the criterion for just compensation is the fair market value of the property at the time of the taking. " 'Fair market value' is defined as the amount in cash, or on terms reasonably equivalent to cash, for which in all probability the property would be sold by a knowledgeable owner willing but not obligated to sell to a knowledgeable purchaser who desired but is not obligated to buy. In ascertaining that figure, consideration should be given to all matters that might be brought forward and reasonably be given substantial weight in bargaining by persons of ordinary prudence, but no consideration whatever should be given to matters not affecting market value" (Standards, pp. 3-4).

Highest and best use. "The determination of the fair market value should include consideration of the highest and best use for which the property is clearly adapted Because the highest and best use is a most important consideration, it must be dealt with specifically in appraisal reports" (Standards, pp. 6-7).

Comparable sales approach. "In the absence of prior sales of the land taken, arm's length transactions in lands in the vicinity of those taken at about the time of taking are the best evidence of market value When there are adequate sales . . . , there is little reason to dwell on other approaches to value to any great extent. . . . Since it is the only approach to value that reflects the balance of supply and demand in actual trading in the market place, it usually develops the most acceptable and convincing evidence of the fair market value of the property" (Standards, p. 9).

Diminution in value due to the proposed project. "[T]he appraisal should include no allowance for . . . diminished value of the property attributable to or resulting from the . . . use or purpose for which the land . . . is to be acquired" (Standards, p. 17).

Results

Analysis of Highest and Best Use

Under existing federal policy, to determine fair market value, each appraisal report is to state the highest and best use that can be made of the property for which there is a current market, and then value the property on the basis of that use (Standards, p. 37).

The first appraisal report provides a detailed analysis of the property leading up to the appraiser's conclusion that the highest and best use of the property is for office, hotel, or mixed commercial and residential development. The second appraisal report, however, contains no mention of the highest and best use of the property.

Analysis of Land Value

Established federal policy requires that the appraiser's opinion of the value of the land shall be supported by confirmed sales of comparable or nearly comparable lands having similar optimum or highest and best uses. Any differences among the comparable lands or between them and the subject property shall be weighed and explained to show how they

indicate the value of the land being appraised (Standards, p. 37). The first appraisal report complies with this policy, whereas in the second appraisal report, the appraiser's opinion of the property's value is not supported as would be required if it were to conform to federal policy.

To support the appraiser's opinion of the property's fair market value the first appraisal report provides a detailed analysis of comparable sales. After examining five comparable sales that took place between December 1986 and October 1988, with adjustments for dates of sale, location, corner influence, zoning, size, configuration, and other factors, the appraiser estimated that the fair market value of the land on October 31, 1988, was \$375 per square foot for a rounded total of \$20,000,000.

The second appraisal report contains no such analysis. Instead, the second appraiser indicates that his opinion is based on "discussions with developers and investors in the West End, as well as (his) research of recent sales . . ." He does not provide any factual data or research that might support his opinion. Federal policy requires that in order to be accorded weight, the appraiser's opinion must be supported with factual data (Standards, p. 42).

Diminution in Value

Federal policy provides that the appraisal should not downgrade the property's value on the basis of the purpose for which the land is to be acquired (Standards, p.17). That is, the fact that the purchaser does not presently plan to develop the property to its highest and best use has no effect under federal policy, or in federal courts, on the value of real property. The first appraisal report complied with this policy, as described above, whereas the second appraisal report was commissioned to base the value of the property on the use for it presently proposed by the Columbia Hospital for Women, which is in fact less than the highest and best use of the property.

The second appraisal report is based on Columbia's proposal to construct a 100,000 square foot office building above grade, and a 112,000 square foot parking garage below grade, on the site. However, like the first appraisal, this appraisal anticipates that the property would most likely be zoned in the C-2-C category which permits a broad range of uses such as an office, hotel, or mixed commercial and residential building. According to both appraisals, if the owner decided to build a mixed commercial and residential building, the total floor to area ratio of the building could be 6.0 to 1—up to 2.0 to 1 for commercial use and 4.0 to 1

for residential use. For example, if the total 53,437 square foot parcel of land in question was available without any building restrictions, such as setback requirements, the owner could construct one or more mixed use commercial and residential buildings containing up to approximately 321,000 square feet—107,000 square feet for commercial use and 214,000 for residential use.

Any development of the property of less than 321,000 square feet would not diminish the value of the land itself because (1) such underdevelopment of the property would be solely at the owner's discretion and would thereby represent an opportunity cost to the owner and (2) the unused development rights could be developed at some later date. For example, the 100,000 square foot office building proposed by the Columbia Hospital for Women will use only 14,000 square feet of the 53,437 square foot lot. The remainder, even though subject to certain restrictions, such as setback requirements, could be used for future residential development.

Conclusion

The two appraisals varied in their approach and differed in their application of the highest and best use standard. The first appraisal adhered to federal policy and determined the fair market value based on the highest and best use standard. In contrast the second appraisal, which did not have to adhere to federal policy, based the market value of the property on the use proposed by the Columbia Hospital for Women—which is less than the highest and best use for the property. We believe that the first appraisal, which was prepared in accordance with federal standards, accurately estimates the fair market value of the property in question. Therefore, we find no justification for revising our original estimate of approximately \$20 million on October 31, 1988.

As arranged with the Subcommittee, unless you publicly announce the contents of this report earlier, we plan no further distribution until 30 days from the date of this letter. At that time, we will send copies to the Administrator of the General Services Administration, the House Committee on the District of Columbia, and other interested parties. We will also make copies available to others on request.

We trust that this analysis responds to your request. If you have any further questions on this matter, please call me on 275-8676.

Sincerely yours,

A handwritten signature in black ink that reads "L. Nye Stevens". The signature is written in a cursive style with a large initial "L" and a long horizontal stroke at the end.

L. Nye Stevens
Director, Government Business
Operations Issues

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